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No. 07-

IN THE

Supreme Court of the United States

COLUMBIA GAS TRANSMISSION CORPORATION,
Petitioner,

v.

RICHARD A. LEVIN
TAX COMMISSIONER OF OHIO
Respondent.

On Petition for a Writ Of Certiorari to the Ohio Supreme Court

PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Interstate natural gas pipeline companies, on the one hand, and local distribution companies, on the other, both use functionally identical pipeline equipment to directly compete in providing many natural gas services in Ohio, but do not directly compete with regard to every service that each offers. Ohio's personal property tax scheme assesses the pipeline equipment at 88% of true value when it is owned by an interstate pipeline company, but at only 25% of true value when the functionally identical equipment is owned by a local distribution company, providing a distinct and systematic competitive advantage to the local distribution companies with regard to those services for which both types of companies compete. This tax scheme gives rise to the following question:

> Are companies that use functionally identical equipment to offer directly competing services in some, but not all, of the markets they serve "similarly situated" for Commerce Clause purposes, so that it violates the Commerce Clause to tax the equipment at a higher rate if it belongs to an interstate company and a lower rate if it belongs to a local distribution company?

PARTIES TO THE PROCEEDING

The petitioner is Columbia Gas Transmission Corporation. The respondent is Richard A. Levin, the Tax Commissioner of the State of Ohio.

RULE 29.6 CORPORATE DISCLOSURE STATEMENT

Petitioner is a wholly-owned subsidiary of NiSource Inc. No publicly-held company owns more than 10% of the stock of NiSource.

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PETITION FOR WRIT OF CERTIORARI

Columbia Gas Transmission Corporation respectfully requests that the Court issue a writ of certiorari to the Supreme Court of Ohio.

OPINIONS BELOW

The decision of the Ohio Tax Department is unreported and is attached at Pet. App. 69a–77a. The decision of the Ohio Board of Tax Appeals is unreported and is attached at Pet. App. 39a–68a. The Ohio Supreme Court's decision is reported at 117 Ohio St. 3d 122 (2008), and is attached at Pet. App. 1a–38a.

JURISDICTION

The Court has jurisdiction under 28 U.S.C. § 1257(a). The Ohio Supreme Court entered its judgment, in which it decided important matters of federal law, on February 14, 2008. The petition was originally due on May 14, 2008. On April 25, 2008, petitioner timely filed a request for an extension of time to file this petition until June 13, 2008. On April 30, 2008, Justice Stevens granted the extension. Petitioner filed this petition before June 13, 2008.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

This case involves the Commerce Clause, Article I, § 8 of the United States Constitution which provides, in pertinent part, that: "The Congress shall have power . . . [t]o regulate commerce with foreign nations, and among the several states, and with the Indian tribes."

STATEMENT

Natural gas heats homes, cooks food, powers industrial equipment, generates electricity, and, more recently, even fuels transportation. Ensuring the efficient delivery of natural gas is an issue of national importance. This case involves a Commerce Clause challenge to a state tax scheme that directly discriminates against interstate commerce in a way that threatens to stymie the development of an effective nationwide natural gas transportation infrastructure. In particular, Ohio taxes natural gas pipeline equipment that is owned by an interstate pipeline company at a rate that is more than three times greater than the rate that is charged if the same equipment is owned by a local distribution company ("LDC").

In upholding this discriminatory state tax scheme, the Ohio Supreme Court adopted a view of the dormant Commerce Clause that conflicts with this Court's precedent and with the decision of at least one other state supreme court. In particular, the court below concluded that it was not enough that Petitioner (an interstate pipeline company) had shown direct competitive harm in the various markets in which interstate pipeline companies directly compete with LDCs in Ohio. Rather, the court found that in order to make out a Commerce Clause claim interstate pipelines must be able to show that they compete with LDCs in one particular market—the market for direct deliveries to residential customers. Any other competition, the Ohio court held, was simply irrelevant for Commerce Clause purposes.

The court purported to rely on *General Motors Corp. v. Tracy*, 519 U.S. 278 (1997), as the basis for this result. In fact, however, the Ohio Supreme Court's per se "you must show that both entities compete in the residential market" requirement contradicts both *Tracy's* language and its logic. Nor can the Ohio court's approach be squared with a recent Kansas Supreme Court decision interpreting *Tracy* in the pipeline context.

Even more troublingly, the decision below provides states virtual impunity to discriminatorily favor LDCs. Because of the prohibitive costs of installing parallel natural gas distribution systems in cities and towns, LDCs will almost always have a natural monopoly on the vast majority of residential transportation service. Thus, a rule that makes significant competition for residential transportation services a necessary prerequisite to a Commerce Clause violation gives states a blank check, both as to discriminatory taxation and (presumably) as to other forms of discriminatory regulation as well.

The potential for such unchecked discrimination threatens to inhibit the development of the nationwide natural gas infrastructure necessary to meet the nation's growing energy needs. Interstate pipelines companies will understandably be leery of spending billions of dollars building new lines, only to find themselves left to compete with local companies on a tilted playing field. And that in turn could well lead to a balkanization of natural gas markets in direct contravention of the longstanding and oft-repeated federal goal of creating and maintaining competitive *nationwide* natural gas markets. Accordingly, Columbia Gas Transmission

Corporation ("Columbia Transmission") respectfully petitions the Court to grant a writ of certiorari and reverse the decision below.

A. The Natural Gas Industry Has Evolved—Local Distribution Companies No Longer Have Captive Customers For Whom They Act As Sole Source Suppliers, And Local Distribution Companies Directly Compete With Interstate Pipeline Companies In Myriad Ways.

Historically, the natural gas delivery industry has included two discrete transportation components. Interstate pipeline companies, such as Petitioner, purchased gas from producers, transported that gas through their pipelines (often across the country) and sold the gas to so-called local distribution companies ("LDCs") at FERC-established rates. See *Tracy*, 519 U.S. at 283-84, and sources cited therein (describing history and development of natural gas industry). These sales were often referred to as "bundled" sales, because the price included both the cost of the gas itself and the cost of transporting that gas to the LDC.

The LDCs in turn sold and transported that gas through their local distribution network to end-user customers, again in the form of a bundled product comprised of the natural gas itself plus the delivery service. Id. The LDCs typically had a local monopoly on end-use distribution in certain geographic areas, but states imposed rate regulations limiting what LDCs could charge for this bundled product, essentially providing the LDCs, like other regulated utilities, a form of cost-plus pricing. Recent regulatory changes, however, have fundamentally changed the face of the natural gas business,

substantially increasing the competition between interstate pipeline companies and LDCs, and also bringing competition to the formerly captive LDC customer base.

1. **Beginning in 1978, Congress largely deregulated the interstate natural gas market.**

In the Natural Gas Policy Act of 1978 (the "NGPA"), Congress began taking steps to increase competition in the natural gas industry, by phasing out the regulation of wellhead prices charged by producers, and encouraging interstate and intrastate pipeline companies to transport natural gas for third parties. *Tracy*, 519 U.S. at 283. The Federal Energy Regulatory Commission ("FERC") continued that process in a series of decisions culminating in Order No. 636, which required interstate pipeline companies to offer gas transportation service on an "unbundled" basis. Id. at 284. As a result, the interstate pipeline companies stopped making wholesale sales of natural gas to LDCs, and began functioning solely as common carriers, using their pipelines to transport gas that LDCs and other customers had acquired directly from producers or other third-party suppliers.

Moreover, the nature of the interstate pipelines' customers changed. Before deregulation, the interstate pipeline companies sold virtually all of their gas to LDCs. Id. at 283. After deregulation, interstate pipeline companies, such as Petitioner, also started selling transportation services to large industrial users that purchased the gas directly from natural gas producers, and then directly connected to the interstate pipeline to receive the gas, rather than

receiving it through the local LDC's distribution network. Id. at 284.

2. Beginning in 1997, Ohio largely deregulated the intrastate natural gas marketplace, and as a result LDCs no longer act as sole-source suppliers to a captive customer base.

Despite these changes in the interstate transportation market, however, the LDCs in Ohio largely continued to operate as they always had, at least with regard to residential customers. To be sure, the LDCs now competed with interstate pipeline companies in selling natural gas transportation services to large industrial users, but the bulk of their business consisted of monopoly sales of the bundled product (i.e., gas plus transportation) to their captive end-user base at a state-regulated rate. Ohio Supreme Court Supp. ("Supp.") at 9-10; 576.

Beginning in 1997, however, Ohio undertook dramatic regulatory changes in the local natural gas distribution market. In particular, the Ohio Public Utility Commission approved LDC "customer choice" programs, through which LDCs unbundled their products—in essence offering access to their distribution networks to competing natural gas suppliers on a common carrier basis. Supp. at 225-26. See also Supp. at 10; 570. Under these programs, consumers were free to purchase their gas from any natural gas marketer or supplier, typically including the LDC, which continued to serve as one of the suppliers for the area. Supp. at 10; 569-70. The consumers then paid a separate transportation

charge to their LDC to transport the natural gas to their home or business. Id.

As a result, much of the LDCs' throughput is now "transportation only." That is, the LDCs' customers purchase their gas from a non-LDC supplier, and use the LDC only for transportation services. To illustrate this, in 1986 only 20% of the gas that LDCs transported through their pipelines in Ohio was carried on a "transportation only" basis. Supp. at 228. By 2005, however, 60% of the gas shipped, Supp. at 228, and at least 50% of the LDCs' residential customers, were "transportation only." Supp. at 118.

More recently, one Ohio LDC, Dominion East Ohio, has requested permission from the Ohio Public Utilities Commission to exit the commodity business entirely and, instead, operate solely as a transport company for its end users. Supp. at 10. If the application is approved, all of the natural gas that moves through that LDC's pipelines would be transportation only, just like the natural gas that moves through interstate pipelines.

In short, Ohio's LDCs no longer act as monopoly sellers offering a bundled product to a captive customer base. Rather, the LDCs are one of many suppliers selling natural gas to customers in a competitive market. To be sure, the LDCs still retain some vestigial obligations from their time as a monopoly supplier, such as an obligation to serve as a provider of last resort. Pet. App. 26a. But the fundamental nature of the residential gas market has changed, replacing the captive-user model with a competition-based market system.

3. Deregulation has led to dramatically increased competition between LDCs and interstate pipeline companies in Ohio.

These dramatic changes in the market have also resulted in greater and ever increasing competition between LDCs and interstate pipeline companies. With regard to the natural gas that is produced and sold in Ohio, of course, the LDCs and interstate pipeline companies like Petitioner can directly compete for transportation services from the wellhead to the delivery point, whether that delivery point is a large industrial direct connect user or another LDC. See, e.g., Supp. at 65-67. Indeed, the record below showed a variety of areas in Ohio where such competition is not merely theoretically possible, but is in fact occurring. Supp. at 7; 69-70; 228-30; 576. The record also showed that LDCs and interstate pipelines directly compete in linking interstate transmission lines to local distribution areas, and in linking distinct distribution areas. Supp. at 443; 449. In all of these activities, customers may choose to move their natural gas through pipelines owned by interstate pipeline companies, or instead through similar pipelines owned by LDCs.

Similarly, as the court below acknowledged, LDCs and interstate pipeline companies also compete for other natural gas related services. Pet. App. at 25a. One example is natural gas storage, in which customers (typically large industrial customers) pay the LDC or interstate pipeline company to ship natural gas to underground sandstone formations where the gas can be stored for delivery at a later time. Supp. at 8; 74-75; 229-30. Another example of a competitive service is natural gas gathering, which

refers to the process of collecting natural gas from the wellhead and preparing it for transportation. Supp. at 11; 451-52. With regard to both types of activities, interstate pipelines and LDCs use functionally identical equipment to directly compete with one another.

B. Ohio's Personal Property Tax Scheme

Ohio imposes a personal property tax on businesses. The tax is computed by multiplying the applicable tax rate (typically expressed as a mill rate) against the assessed value of the company's personal property. Accordingly, the higher the assessed value, the higher the tax paid.

With regard to pipeline equipment, Ohio's tax code specifies two different assessment rates depending on whether the pipeline equipment is owned by a "natural gas company" or a "pipe-line company," both of which are statutorily defined terms. The statutes define a natural gas company as any company that is "engaged in the business of supplying or distributing natural gas for lighting, power, or heating purposes to consumers within [Ohio]." OHIO REV. CODE ANN. § 5727.01(D)(4) (West 2007). A "pipe-line company," on the other hand, is defined as any company "engaged in the business of transporting natural gas, oil, or coal or its derivatives through pipes or tubing, either wholly or partially within this state." OHIO REV. CODE ANN. § 5727.01(D)(5) (West 2007).

Property belonging to a "natural gas company" is assessed at 25% of true value. OHIO REV. CODE ANN. § 5727.111(C) (West 2007). Property belonging to a "pipe-line company," by contrast, is assessed at 88% of true value. OHIO REV. CODE ANN. § 5727.111(D) (West 2007). Thus, a "pipe-line company" pays over

three times the tax that a "natural gas company" pays on the same kind of pipeline equipment.

C. Columbia Transmission's Challenge To The Discriminatory Tax Scheme

The Ohio Department of Taxation assessed Columbia Transmission's property at the 88% rate, contending that Columbia Transmission qualified as a "pipe-line company." Pet. App. 2a. Columbia objected to that assessment, claiming that while it met the statutory definition of a "pipe-line company," it also met the definition of "natural gas company," and that, as it met both definitions, it was free to elect either classification. Pet. App. 55a. The Department rejected that contention, however, asserting that (1) while Columbia admittedly supplied natural gas to consumers in Ohio—i.e., the statutory definition of a natural gas company—Columbia's *primary* business was transporting natural gas, and (2) that the statutory definition tacitly included a "primary business" test. Pet. App. 3a–4a, 59a.

Columbia appealed the Department's determination to the Ohio Board of Tax Appeals, pressing various statutory and constitutional claims, including a dormant Commerce Clause claim.[1] Pet. App. 43a–44a. The Board reversed the Department's determination on statutory grounds, finding that Columbia met the statutory definition of a "natural

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[1] Ohio law precludes the Board of Tax Appeals from considering constitutional claims. See *MCI Telecomms. Corp. v. Limbach*, 68 Ohio St.3d 195 (1994). Taxpayers are nonetheless required to present their constitutional claims to the Board, or those claims are deemed waived. Id. at 197-99.

gas company" and thus was entitled to the lower assessment rate. Pet. App. 66a–67a.

The Department appealed the Board's ruling to the Ohio Supreme Court, again claiming that Columbia Transmission was a "pipe-line company" rather than a "natural gas company." Pet. App. 4a. In response, Columbia argued, inter alia, that the Department's approach results in LDCs uniformly receiving the preferable tax treatment, and interstate pipeline companies uniformly being taxed at the higher rate. It further noted that this tax differential imposes a competitive disadvantage on interstate pipeline companies in the various markets, and with regard to the various services, in which they compete head to head with LDCs. Accordingly, Columbia argued that, if interpreted to systematically disadvantage the interstate pipelines in their competition with LDCs, the tax scheme would violate the dormant Commerce Clause. Pet. App. 19a.

The Ohio Supreme Court reversed the Board of Tax Appeals and imposed the higher assessment rate. Pet. App. 37a. In doing so, the court rejected Columbia's Commerce Clause argument. Pet. App. 29a. The court based its rejection of that argument on its determination that interstate pipeline companies and LDCs are not "similarly situated" for Commerce Clause purposes. Pet. App. 22a. In reaching that conclusion, the court acknowledged that the question of whether groups are "similarly situated" under the Commerce Clause typically turns on whether there is "actual or prospective competition between the supposedly favored and disfavored entities in a single market." Id. And the court did not dispute that the

interstate pipelines and LDCs competed with regard to various services. Pet. App. 25a.

The court read this Court's decision in *GM v. Tracy*, however, as essentially adopting a special dormant Commerce Clause rule for natural gas markets, under which it is not enough for a company to show that it competes with LDCs in one or more markets, but rather the *only* relevant question is whether the company competes with the LDC *in the residential distribution market*. Pet. App. 25a–27a, 28a. In the Ohio court's view, *Tracy* means that no other competition matters: "In conclusion, Columbia's failure to show that it is in direct competition with Ohio LDCs *in the residential market* proves fatal to its dormant Commerce Clause claim." Pet. App. 29a. Of course, as LDCs have a natural monopoly on residential distribution (given the expense of building a competing distribution network in cities), the Ohio Supreme Court's ruling means that states will be free to provide their in-state LDCs with a competitive advantage over interstate pipeline companies in the many competitive markets in which both operate.

Given the impediments that such discriminatory taxation creates for Columbia Transmission's ability to compete with LDCs, Columbia Transmission now respectfully urges the Court to grant certiorari to review the Ohio Supreme Court decision.

REASONS FOR GRANTING THE WRIT

I. THE DECISION BELOW CONFLICTS WITH *GM v. TRACY* AND THE COURT'S COMMERCE CLAUSE JURISPRUDENCE IN GENERAL.

The Ohio Supreme Court, while purporting to apply *GM v. Tracy*, failed to appreciate the context in which that case was decided. As a result, its decision, far from finding justification in *Tracy*, actually conflicts with the Commerce Clause principles that *Tracy* elucidates. In particular, *Tracy* created a narrow exception to the Commerce Clause's general prohibition on state taxes that create a competitive advantage for local companies—an exception the Court based solely on the unique role that local distribution companies then played as the monopoly supplier of natural gas to a captive residential customer base. That role has now ended, and thus so should the exception. The court below, however, read *Tracy* to permanently engraft into the Commerce Clause permission for states to favor local distribution companies in their taxation schemes. That result conflicts with *Tracy's* reasoning and this Court's dormant Commerce Clause jurisprudence generally, serves to improperly ossify a Commerce Clause jurisprudence that must be free to react to market changes, and threatens to forestall development of necessary natural gas infrastructure in direct contravention of Congress's stated policy goals.

A. The Commerce Clause prohibits discrimination between "similarly situated" entities.

It is well-settled that states cannot use their tax systems (or other regulatory systems) to engage in "economic protectionism—that is, regulatory

measures designed to benefit in-state economic interests by burdening out-of-state competitors." *New Energy Co. v. Limbach,* 486 U.S. 269, 273 (1988). Stated alternatively, "[t]he negative or dormant implication of the Commerce Clause prohibits state taxation, or regulation, that discriminates against or unduly burdens interstate commerce and thereby impedes free private trade in the national marketplace." *Tracy,* 519 U.S. at 287 (quotations and citations omitted). To that end, "[a] discriminatory law is virtually per se invalid..." *Dep't. of Revenue of Ky. v. Davis,* ____U.S. ____, Slip. Op. at 8 (May 19, 2008) (quotations and citations omitted).

As this Court noted in *Tracy,* however, the "threshold question," see 519 U.S. at 299, is whether the two differentially treated companies are "similarly situated" for Commerce Clause purposes. This is so because "[c]onceptually, of course, any notion of discrimination assumes a comparison of substantially similar entities." Id. at 298.

The *Tracy* Court defined "substantial similarity," in turn, by reference to the goals that the Commerce Clause is designed to achieve. In particular, the Commerce Clause seeks to foster free competition in order to protect "markets and participants in markets." Id. at 300. Substantial similarity, then, turns on whether the two entities compete in at least one market—"in the absence of actual or prospective competition between the supposedly favored and disfavored entities in a single market there can be no local preference, whether by express discrimination against interstate commerce or undue burden upon it, to which the dormant Commerce Clause may apply." Id. Litigants seeking to lay claim to

Commerce Clause protection, then, must show that they have suffered a competitive harm as a result of a preferential advantage conferred by the state.

B. *Tracy's* determination that LDCs were not "similarly situated" to independent gas marketers was driven exclusively by the fact that LDCs served as monopoly suppliers to a captive residential market, a fact that is no longer true.

In *Tracy*, the Court considered the application of these principles to an Ohio sales tax that exempted LDCs, but not interstate natural gas marketers, from sales tax liability for sales of natural gas. The way the natural gas market was structured during the late-80's timeframe (the period at issue in *Tracy*, see id. at 282 n.1), the two groups directly competed in selling natural gas in unregulated transactions at market-based prices to large industrial companies. But the LDCs at that time still served as monopoly providers of bundled gas sales at regulated prices (and regulated terms) to the noncompetitive, captive residential market. Id. at 302-03. In ascertaining whether the two groups were similarly situated, the Court thus had to determine whether to "accord controlling significance to the noncaptive market in which [the two groups] compete, or to the noncompetitive, captive market in which the local utilities alone operate." Id. at 303-04.

The Court focused on the latter market and thus determined that the groups were not similarly situated for Commerce Clause purposes, but it did so based exclusively on concerns about the impact that its ruling would have on *the LDCs' role as monopoly suppliers to a captive residential market*—a condition

that no longer exists in Ohio. In essence, the Court concluded that the LDCs' status as monopoly suppliers of bundled gas to a non-competitive, captive market required an exception to the typical Commerce Clause rules that would otherwise apply.

To that end, the Court noted both the long history of state regulation of the non-competitive captive market, as well as the tacit congressional approval for those state regulatory regimes—observing that "Congress has done nothing to limit its unbroken recognition of the state regulatory authority that has created and preserved the local monopolies." Id. at 304-05. Given this history, the Court recognized "[t]he continuing importance of the States' interest in protecting the captive market from the effects of competition," and concluded that this was a "legitimate state interest" that was "compatible with the Commerce Clause." Id. at 306. Cf. *Oregon Waste Sys., Inc. v. Dep't. of Env't Quality*, 511 U.S. 93, 101 (1994) (observing that even discriminatory laws can survive if they "advance[ ] a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives"). (quotation and citation omitted).

Similarly, the Court noted that it lacked the institutional expertise to correctly assess the impact that applying the Commerce Clause's typical non-discrimination standard would have on LDCs' provision of the bundled service to the captive market. Observing that "the Court is institutionally unsuited to gather the facts upon which economic predictions can be made," 519 U.S. at 308, the Court concluded that "[t]he most we can say is that modification of Ohio's tax scheme could subject LDCs

to economic pressure that in turn could threaten the preservation of an adequate customer base to support continued provision of bundled services to the captive market." Id. at 309. Based on such concerns, the Court concluded that the LDCs, which principally sold "noncompetitive bundled gas," were not similarly situated to interstate suppliers.

In short, the *Tracy* Court used the "substantial similarity" label to balance the competitive harms that the discriminatory tax would cause marketers in the competitive markets, against the States' "legitimate interest" in preserving and protecting the non-competitive, captive residential market. And the Court found that the legitimate interest in protecting the latter would in effect offset what would otherwise have been a Commerce Clause violation. Cf. *Oregon Waste Sys.*, 511 U.S. at 101 (discrimination acceptable if it advances a "legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives").

C. The decision below expands *Tracy* far beyond its original bounds and creates a blank check for State discrimination in favor of LDCs.

The court below here, while purporting to rely on *Tracy*, arrived at a result that is fundamentally inconsistent with *Tracy's* underlying economic rationale. In particular, failing to appreciate the importance of the "noncompetitive, captive market," 519 U.S. at 303, to *Tracy's* analysis, the court below interpreted the case to create a per se rule that two competitors in the natural gas industry cannot be "similarly situated" for Commerce Clause purposes unless they directly compete against each other in the residential market. The court reached that result

even though Ohio's residential market is no longer captive, but is instead fully competitive. The court below thus transformed *Tracy's* subtle balancing test into a blunt instrument that allows virtually unchecked discrimination in favor of LDCs.

Importantly, the Ohio Supreme Court did not dispute that LDCs and interstate pipeline companies (such as Petitioner) do directly compete with regard to a variety of natural gas services. According to the court, however, any such competition was of no moment in the Commerce Clause analysis for one reason—as a matter of law the two entities could not be "similarly situated" unless both entities competed in the residential natural gas market: "In conclusion, Columbia's failure to show that it is in direct competition with Ohio LDCs in the residential market proves fatal to its dormant Commerce Clause claim." Pet. App. 29a.

The court reached this result even after recognizing that the residential market in Ohio is now fully competitive, and the LDCs have unbundled gas and transport services. In the court's words, "LDCs now offer both bundled and unbundled services and, as Columbia notes, they can sell natural gas, transportation service, and storage service separately." Pet. App. 27a. According to the court, though, it was not enough to escape *Tracy's* shadow that the LDCs' local market was now competitive, rather the competition in that market had to come *from the interstate pipeline companies themselves* in order to make out a Commerce Clause violation:

> Nevertheless, the main competitors of LDCs in the residential and small-business markets are not interstate-pipeline companies. Rather,

> independent and LDC-affiliated marketers compete with LDCs for commodity sales in this market. Moreover, marketers largely rely on the LDC's distribution network to deliver their natural gas to end-use customers. In other words, interstate-pipeline companies do not compete for residential and small-business customers for either natural gas sales or transportation services.

Id.

This requirement—that the residential market must be competitive and that the competition must come directly from the interstate pipelines themselves—goes well beyond *Tracy*. As noted above, *Tracy* rested on concerns regarding the "noncompetitive, captive market," a market that no longer exists. Ohio's residential consumers now have the ability to pick their natural gas supplier from a host of competitors. Indeed, at least one LDC has sought to exit the supplier business entirely and act solely as a transport company, meaning it would not sell the bundled product *at all*. Supra at 7. Accordingly, the "legitimate state interest" that *Tracy* allowed to insulate a discriminatory tax from Commerce Clause scrutiny is no more and cannot be invoked as a basis for sustaining Ohio's discriminatory property tax scheme here.

Absent *Tracy's* protection, though, the decision below directly contradicts the Court's well-settled Commerce Clause principle that States may not "tax a transaction or incident more heavily when it crosses state lines than when it occurs entirely within the state." *Armco, Inc. v. Hardesty*, 467 U.S. 638, 642 (1984). See also, e.g., *Oregon Waste Sys.*,

511 U.S. 93, 99 (1994) (calling this principle "well established"); *Camps Newfound/Owatonna, Inc. v. Town of Harrison*, 520 U.S. 564, 581 (1997) (quoting *Armco*); *Fulton Corp. v. Faulkner*, 516 U.S. 325, 331 (1996) (same). The Ohio tax plainly imposes just such a forbidden tariff.

Although most of the natural gas produced in the United States comes from the states of Texas, Oklahoma, and Louisiana, a significant amount of gas is produced in Ohio. Supp. at 679. In fact, Ohio ranks 18th among the states in natural gas production. Supp. at 233. Therefore, when Ohio LDCs or other natural gas suppliers acquire gas for resale to residential and other retail customers, they have a choice; they may purchase gas from local, Ohio producers or from out-of-state producers or suppliers. Supp. at 456. In many instances, given the configuration of natural gas pipelines in Ohio, it is possible to transport locally-produced, Ohio gas from the point of acquisition to a customer's home or business using only the intrastate facilities of one or more LDCs. Supp. at 229; 450-453; 687. Purchases of gas from out-of-state suppliers for consumption in Ohio, on the other hand, as well as sales of Ohio gas to out-of-state purchasers, must necessarily be transported by an interstate pipeline company. Thus, gas that remains "entirely within the state" can be transported at a lower effective tax rate than gas that crosses Ohio's borders, effectively imposing a tariff and also granting Ohio's LDCs a competitive edge in their competition for in-state transportation.

This is precisely the type of "economic protectionism" that the Commerce Clause prohibits. Indeed, the Court has called such discrimination

"virtually per se invalid," *Oregon Waste Sys.*, 511 U.S. at 99.

In short, the Ohio taxation scheme systematically disadvantages interstate pipeline companies in competing with LDCs. The Ohio Supreme Court's refusal to recognize a Commerce Clause violation on the facts below cannot be squared with the Court's Commerce Clause precedent.

II. THE DECISION HERE CONFLICTS WITH *IN RE CIG FIELD SERVICES COMPANY*, 279 KAN. 857 (2005).

Not only does the decision here directly conflict with *Tracy* and the Commerce Clause principles it elaborates, it also conflicts with *In re CIG Field Services Co.*, 279 Kan. 857 (2005), in which the Kansas Supreme Court applied *Tracy* in the natural gas pipeline context. This conflict provides a second basis warranting review.

In *In re CIG*, the Kansas Supreme Court struck down on Commerce Clause grounds a state tax statute that assessed property owned by interstate and intercounty gas gathering systems at one rate (33% of fair market value), and property owned by intracounty gas gatherers at a more favorable rate (25% of fair market value). 279 Kan. at 859. The court recognized that under *Tracy* the first question was whether the two differently treated groups were "similarly situated." Id. at 867. In answering that question, though, the court did not limit its inquiry, as the Ohio Supreme Court did here, to whether the two groups competed in the residential market. Nor did the court suggest that it was necessary to show that the two groups competed in every market in which each operated. Rather, the question was

merely whether the two groups engaged in "actual or prospective competition," see id. (quoting *Tracy*), in such a way that "the statute's discrimination affects the systems' economic choices in competitive markets," see id. at 868. Because the different types of entities competed in at least some of the markets they served, the court concluded that they were "similarly situated" for Commerce Clause purposes. Id. at 869.

Applying the Kansas Supreme Court's approach here, of course, would have resulted in a finding that the interstate pipeline companies and LDCs are "similarly situated." The record evidence clearly shows, and the Ohio Supreme Court did not dispute, that interstate pipeline companies and LDCs directly compete in many of their activities, and that the differential taxation would thus necessarily "affect[ ] the systems' economic choices in competitive markets." 279 Kan. at. 868. It was only as a result of the Ohio court's single-minded focus on the residential market, a focus decidedly absent in *In re CIG*, that the court concluded the groups were not "similarly situated." Only this Court can resolve which of these two inconsistent understandings of "similarly situated" under the Commerce Clause is correct, and Columbia Transmission urges the Court to use this case as a vehicle to do so.

III. THE DECISION BELOW CONTRAVENES CONGRESS'S GOAL OF MAINTAINING A UNIFORM NATIONWIDE NATURAL GAS MARKET AND THREATENS TO UNDERMINE THE DEVELOPMENT OF NECESSARY NATURAL GAS INFRASTRUCTURE.

Not only does the decision below create a clear conflict with this Court's decisions, as well as the decision of another state supreme court, but it does so in an area of exceptional national importance. No one can doubt that energy infrastructure issues have taken on increased significance in recent years and particularly now, and on that front, the Ohio court's decision threatens to undermine Congress's stated policy goal of achieving a uniform nationwide natural gas market.

Natural gas is a vital component of our country's energy resources, an importance that only continues to grow as the cost of oil rises. In assessing how best to meet the country's natural gas needs, both Congress and the FERC have often stated their belief that America's natural gas markets are best served by a uniform nationwide marketplace in which competitors across the country compete on an even playing field.

One driver behind the Natural Gas Policy Act of 1978, for example, was Congress's desire to create a competitive nationwide marketplace. See *Tracy,* 519 U.S. at 816. See also S. Rep. No. 436, 95th Cong., 1st Session 21 (1977) (noting the need to eliminate "the interstate-intrastate distinction ... together with the resulting distorting effect on both production and distribution"). Similarly, in issuing Order No. 636, which mandated that interstate pipelines unbundle

transportation and the sale of gas, (essentially forcing pipeline companies to serve as common carriers) FERC expressly noted its goal of creating a "competitive, national market":

> "This rule will therefore reflect and finally complete the evolution to competition in the natural gas industry initiated by those changes so that all natural gas suppliers, including the pipeline as merchant, will compete for gas purchasers on an equal footing."
>
> * * *
>
> "The first goal is to ensure that all shippers have meaningful access to the pipeline transportation grid so that willing buyers and sellers can meet in a competitive, national market to transact the most efficient deals possible."

Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation and Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol, Order No. 636, 57 Fed. Reg. 13,267 (1992), F.E.R.C. Stats. and Regs., Regulations Preambles January 1991-June 1996 ¶ 30,939 at 30,391, 30,393 (April 8, 1992) (subsequent history omitted).

And six months later, when it amended Order 636, FERC again noted the need to "ensure there is no obstacle to the consumers' access to a natural gas pipeline grid and to the blossoming national gas market." Order No. 636-A., 57 Fed. Reg. 36,128 (1992), F.E.R.C. Stats. and Regs., Regulations Preambles January 1991 - June 1996 ¶ 30,950 at 30,538 (August 3, 1992) (subsequent history omitted). More recently, the FERC has noted its interest in

"standardiz[ing] the business practices and communication methodologies of interstate pipelines in order to create a more integrated and efficient pipeline grid." *Standards for Business Practices of Interstate Natural Gas Pipelines,* Order No. 587-S, 70 Fed. Reg. 28,204 (2005), 70 Fed. Reg. 37,031 (2005), F.E.R.C. Stats and Regs., Regulations Preambles ¶ 31,179 at 31,396 (June 28, 2005). And only six months ago, the Commission again stated its desire to ensure a "competitive, national market." *Promotion of a More Efficient Capacity Release Market,* 72 Fed. Reg. 65,916 (2007), F.E.R.C. Stats. and Regs., Proposed Regulations Preambles ¶ 32,625 at 33,410 (November 15, 2007).

Developing and maintaining this "competitive, national market" will require a new and improved natural gas infrastructure, a fact that both Congress and the FERC have explicitly recognized. In the Energy Policy Act of 2005 (EPAct 2005), Pub. L. No. 109-58, 119 Stat. 594 (2005), Congress enacted several provisions designed to encourage both the construction of new energy facilities and the improvement of existing ones. Section 1241 of EPAct 2005, for example, directed FERC to establish incentive-based rate treatments that promote investment in electric transmission facilities. Section 311 gave FERC exclusive authority to approve applications for the siting, construction, expansion, or operation of liquefied natural gas (LNG) terminals. Section 1263 repealed the Public Utility Holding Company Act of 1935, which was thought to be a disincentive to investment in energy infrastructure. And Section 312 authorized FERC to allow interstate pipeline companies, such as Petitioner, to charge market-based (as opposed to cost-based) rates for new

natural gas storage capacity—even if the company cannot demonstrate that it lacks market power—where, among other things, those rates are necessary to encourage the construction of storage capacity in areas needing additional storage services.

In enacting Section 312 of EPAct 2005, Congress specifically recognized the important role that underground natural gas storage facilities, such as those owned and operated by Petitioner and other interstate pipeline companies (and LDCs), play in meeting the nation's energy needs. That role is twofold. First, as FERC explained in its order implementing the provisions of Section 312, storage is "critical in assuring that overall demands and specific requirements of natural gas customers are met." *Rate Regulation of Certain Natural Gas Storage Facilities,* Order No. 678, 71 Fed. Reg. 36,612 (2006), F.E.R.C. Stats. and Regs., Regulations Preambles ¶ 31,220 at 30,408 (June 19, 2006). Since gas usage increases significantly during the colder winter months, withdrawals from storage are needed to meet ongoing demand that cannot be satisfied with flowing gas supplies from current production. One estimate cited by FERC indicated that the combined energy needs of the United States and Canada will require an additional 700 billion cubic feet of storage capacity by 2025. Id. at 30,409.

Second, as FERC went on to explain, "[s]torage can have a moderating influence on gas prices." Id. This occurs because gas storage functions as a physical hedge. Customers can build up inventories during periods of lower demand, and later rely on those supplies instead of paying high spot market prices. Id. In fact, a FERC report concluded that storage

"may be the best way of managing gas commodity price[s] . . ." Id.

As a result of these considerations, FERC made various changes to its regulations "in order to facilitate the development of new natural gas storage capacity to ensure that adequate storage capacity will be available to meet anticipated market demand and to mitigate natural gas price volatility." Id.

In offering natural gas storage services, however, Petitioner and other interstate pipeline companies operating in Ohio must compete directly with local gas distribution companies, such as Dominion East Ohio. Supp. at 8. Although these companies operate storage facilities that are functionally equivalent to those operated by interstate pipeline companies, they are nonetheless classified as "natural gas companies" under the Ohio statutes, and their property is therefore taxed at 25% of true value, rather than the 88% rate which applies to interstate pipeline company property.

The Ohio Supreme Court's decision allowing unfettered discrimination against Petitioner and other companies doing business in interstate commerce runs directly counter to the incentives provided by Congress and FERC, and significantly inhibits the ability of these companies to construct and operate new natural gas pipelines, storage capacity, and other facilities needed to meet the nation's growing energy needs. Indeed, as noted above, Ohio's tax essentially acts as a tariff—gas produced in Ohio that remains in Ohio can be shipped through LDC-owned pipelines, and thus bear a lower effective tax rate than Ohio gas shipped into interstate commerce or out-of-state gas shipped into

Ohio. And with regard to competitive services such as gas storage, the discriminatory impact will be even more directly felt, as the Ohio LDCs will be able to pass along the discriminatory tax savings to their customers, thereby directly undercutting the interstate pipeline companies' competitive efforts.

If other states adopt similar taxes, the balkanizing effect of such discrimination will only increase. The "integrated and efficient pipeline grid" that Congress had envisioned as creating a uniform nationwide market could well be replaced by a patchwork quilt of intrastate pipelines, thereby frustrating the movement of natural gas across state lines.

And the threat of these discriminatory taxes spreading beyond Ohio is not merely theoretical. Already both Kansas and Louisiana have sought to impose taxes that treat interstate companies more harshly than local competitors. See *In re CIG Field Services Co.,* 279 Kan. 857 (2005); *ANR Pipeline Co. v. Louisiana Tax Commission,* 923 So. 2d 81 (La. App. 2005) (discussing Louisiana Tax Commission's efforts to use a different methodology to assess intrastate pipeline companies than interstate pipeline companies). Nor are the states' efforts in that regard surprising. Interstate pipeline companies typically operate (as there name suggests) in many states and thus often lack significant political capital in any one particular state, especially as compared to their more local competitors. Similarly, a heightened tax on interstate pipelines is politically attractive, as the costs of such a tax are to some extent born by the interstate pipeline company's consumers, who are often not even residents of the taxing state. In light of such pressures, decisions like the one below will only

embolden legislators to enact even more such discriminatory taxes.

In sum, the Ohio Supreme Court's decision creates substantial impediments for the development of an "integrated and efficient pipeline grid" and thus interferes with Congress's goal of developing a "competitive, national market." Given these significant and perhaps irrevocable consequences on this issue of national importance, as well as the conflicts the decision below creates, Columbia Transmission respectfully urges the Court to grant certiorari and reverse the Ohio Supreme Court's decision.

CONCLUSION

For the above-stated reasons, the Court should grant the petition for a writ of certiorari.

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